

**HARRIS COUNTY
IMPROVEMENT DISTRICT NO. 1**

**ANNUAL FINANCIAL AND
COMPLIANCE REPORT**

**Year Ended June 30, 2015
with Independent Auditor's Report**

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

FINANCIAL REPORT

Year Ended June 30, 2015

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INDEPENDENT AUDITOR'S REPORT

Board of Directors
Harris County Improvement District No. 1
Houston, Texas

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities and each major fund of Harris County Improvement District No. 1 (the "District") as of and for the year ended June 30, 2015, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and each major fund of the District as of June 30, 2015, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 5 through 12 and the Schedule of Revenues, Expenditures and Changes in Fund Balance – Budget to Actual on pages 34 through 35 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other information

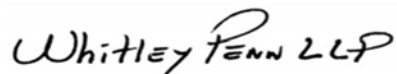
Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the District's basic financial statements. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements.

The schedule of expenditures of federal awards is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Board of Directors
Harris County Improvement District No. 1

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated January 18, 2016, on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting and compliance.

A handwritten signature in black ink that reads "Whitley Penn LLP". The signature is written in a cursive, flowing style.

Houston, Texas
January 18, 2016

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MANAGEMENT'S DISCUSSION AND ANALYSIS

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HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

MANAGEMENT'S DISCUSSION AND ANALYSIS

Year Ended June 30, 2015

As management of the Harris County Improvement District No. 1 (the "District"), we offer readers of the District's financial statements this narrative overview and analysis of the financial activities of the District for the fiscal year ended June 30, 2015. The fiscal year starts on July 1, 2014 and ends on June 30, 2015.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the District's basic financial statements. The District's basic financial statements comprise three components: (1) government-wide financial statements, (2) fund financial statements and (3) notes to the financial statements. This report also contains required supplementary information in addition to the basic financial statements themselves.

Government-wide Financial Statements

The government-wide financial statements are designed to provide readers with a broad overview of the District's finances, in a manner similar to a private-sector business.

The *Statement of Net Position* presents information on all of the District's assets and liabilities, and deferred outflows of resources with the difference reported as net position. Over time, increases or decreases in net position may serve as a useful indicator regarding the financial position of the District. Other factors that are not included in the financial statements, such as increased tax base in the District's boundaries, should be considered in evaluating the condition of the District's overall financial position.

The *Statement of Activities* presents information showing how the government's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

Fund Financial Statements

A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The District, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

The District maintains three individual governmental funds. Information is presented separately in the *Governmental Fund Balance Sheet* and in the *Governmental Fund Statement of Revenues, Expenditures and Changes in Fund Balances* for the General Fund, the Debt Service Fund, and the Capital Projects Fund, all of which are considered to be major funds.

Fund financial statements are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements. Because the focus of governmental funds is narrower than that of the government-wide financial statements, it may be useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's near-term financing decisions. Both the *Governmental Fund Balance Sheet* and the *Governmental Fund Statement of Revenues, Expenditures and Changes in Fund Balances* provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

MANAGEMENT’S DISCUSSION AND ANALYSIS (continued)

Notes to the Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

Government-wide Financial Analysis

In the government-wide statements, the difference between assets and deferred outflows and liabilities is called net position. As previously noted, net position may serve over time as a useful indicator of a government’s financial position. The District’s net position at June 30, 2015, was \$39,152.

Net position is categorized based on the availability to provide financial resources for the District. Net position that is “Invested in capital assets, net of related debt” represent the District’s investments in capital assets, less any debt used to acquire those assets that is still outstanding. Resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities. “Restricted” net position represents amounts that are restricted for future debt service requirements. “Unrestricted” net position represents amounts available to meet the District’s future obligations.

At year-end, the District had total assets of \$9,974,952 and deferred outflows of \$164,614. Of this amount, \$7,170,673 consisted of cash and cash equivalents and \$1,800,256 of capital assets. The change in capital assets consisted of depreciation of \$745,959. Total liabilities were \$10,100,414 as of year-end. Of this amount, \$8,378,451 consisted of long-term debt and accrued interest. The balance of the liabilities consists of accounts payable and other accrued liabilities and expenses. A comparative summary of the District’s overall financial position, as of June 30, 2015 and 2014, is as follows:

	2015	2014
Current and other assets	\$ 8,174,696	\$ 7,701,209
Capital assets	1,800,256	1,992,513
Total Assets	9,974,952	9,693,722
Deferred Charge on Refunding	164,614	184,750
Total Deferred outflows	164,614	184,750
Other liabilities	1,801,723	2,167,948
Long-term liabilities	8,298,691	9,141,953
Total Liabilities	10,100,414	11,309,901
Net position:		
Investment in capital assets	1,800,256	1,992,513
Restricted	1,148,835	1,128,284
Unrestricted	(2,909,939)	(4,552,226)
Total Net Position	\$ 39,152	\$ (1,431,429)

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Government-wide Financial Analysis - continued

The total net position of the District increased by \$1,470,581. A comparative summary of the District's statement of activities for the past two years is as follows:

	<u>2015</u>	<u>2014</u>
Revenues		
Program revenue		
Charges for services	\$ 1,418,232	\$ 1,007,886
Capital Grants	4,688,550	3,342,906
General revenues		
Property taxes	7,619,248	6,388,676
Unrestricted investment earnings	15,723	14,284
Total Revenues	<u>13,741,753</u>	<u>10,753,752</u>
Expenses		
General and administrative	2,804,728	2,547,615
Traffic control	1,739,788	1,684,702
Maintenance and beautification	1,781,585	1,839,684
Planning and engineering	138,446	1,801,038
Marketing and communications	787,931	354,510
Interest on long-term debt	239,644	315,609
Economic development	90,500	72,520
Transfers to other governments	4,688,550	1,773,059
Total Expenses	<u>12,271,172</u>	<u>10,388,737</u>
Increase (decrease) in net position	1,470,581	365,015
Net position - beginning	(1,431,429)	(1,796,444)
Net position - ending	<u>\$ 39,152</u>	<u>\$ (1,431,429)</u>

Financial Analysis of the Government's Funds

The focus of the District's governmental funds is to provide information on near-term inflows, outflows, and balances of spendable resources. Such information is useful in assessing the District's financing requirements. In particular, unassigned fund balance may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

As of the end of the current fiscal year, the District's governmental funds reported combined ending fund balances of \$7,114,060, an increase of \$873,033 in comparison with the prior year. This is due to increase in property tax revenues. The unassigned portion of fund balance is \$5,860,840. This amount is available for spending at the government's discretion. The remainder of fund balance is restricted to indicate that it is not available for new spending because it has already been committed to pay debt service of \$1,198,453 and nonspendable fund balance of \$54,767 related to prepaid items.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

Financial Analysis of the Government's Funds - continued

The following is a summary of changes in fund balances for the prior two fiscal years:

	2015	Increase (Decrease)	2014	Increase (Decrease)	2013
General Fund	\$ 6,167,986	\$ 860,894	\$ 5,307,092	\$ 107,147	\$ 5,199,945
Capital Projects Fund	(252,379)	1,132	(253,511)	1,140	(254,651)
Debt Service Fund	1,198,453	11,007	1,187,446	(11,662)	1,199,108
	<u>\$ 7,114,060</u>	<u>\$ 873,033</u>	<u>\$ 6,241,027</u>	<u>\$ 96,625</u>	<u>\$ 6,144,402</u>

The General Fund is the chief operating fund of the District. Fund balance in the General Fund increased by \$860,894 during the current fiscal year. This increase is due to increases in property tax revenues. As a measure of the General Fund's liquidity, it may be useful to compare unassigned fund balance to total fund expenditures. At the end of the current fiscal year, the unassigned portion of fund balance of the General Fund was \$6,113,219, while expenditures for the year were \$6,585,260.

The Debt Service Fund has a total fund balance of \$1,198,453, all of which is restricted for the payment of debt service. The increase in fund balance during the current year in the Debt Service Fund was \$11,007.

The Capital Projects Fund has a total deficit of \$252,379. The decrease in the deficit in fund balance during the current year in the Capital Projects Fund of \$1,132 is related to the transfer of grant funds to the Uptown Development Authority for transit related projects.

General Fund Budgetary Highlights

The Board of Directors did not amend the budget during the year. The District anticipated an increase in the fund balance of \$1,061,707, while the actual was an increase of \$860,894. Variances between budget and actual were due primarily to budget variances in property tax revenues and operational spending.

Debt Administration

At June 30, 2015 and 2014, the District had total bonded debt outstanding as shown below:

Series	2015	2014
Series 2013	8,505,000	9,255,000
	<u>\$ 8,505,000</u>	<u>\$ 9,255,000</u>

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

MANAGEMENT'S DISCUSSION AND ANALYSIS (*continued*)

Economic Factors and Next Year's Budgets and Rates

The District is a political subdivision of the State of Texas, created in 1987 by a special act of the 70th Texas Legislature. The District levies an ad valorem tax on real and personal property within its boundaries. The tax rate for tax year 2014 was \$0.14345 per \$100 of assessed value. The tax rate will remain the same for tax year 2015, with expected revenues of approximately \$5.78 million.

Office Space

Uptown Houston is one of the largest business districts outside a historic core in the United States. It is the 15th largest business district in the United States: comparable to Denver and Cleveland. With almost 24 million square feet of total office space in its market area, Uptown accounts for over 13% of Houston's total 'Class A' office space with 17 million square feet. There are over 96,000 office employees in the Uptown area. At the end of the fiscal year, class A office space was 88% leased.

Overall, 2015 certified ad valorem values for the office sector were approximately 7% higher than 2014 values. Last fiscal year, Uptown celebrated two new additions to the office sector: the BBVA Compass Plaza at 2200 Post Oak Boulevard and 3009 Post Oak Boulevard. During this fiscal year, BHP Billiton's new 30-story office building on Post Oak Boulevard is about 67% percent complete. This will be BHP's new global headquarters and will house between 2,000 to 3,000 employees. The project is expected to be completed late 2016. In addition, the broader Uptown market area saw Amegy Bank break ground on its 350,000 square foot office building as well as Nelson-Murphree's groundbreaking for its 165,000 square foot office tower.

Retail

Uptown is synonymous with shopping and is known as a world-renowned center for retail. Ad valorem values for the retail sector were certified over 6% higher 2015. Retail was 99% leased as of 2015. This market maintained as The Galleria is now the fourth largest retail center in the United States. The newest 22-acre mixed-use development known as BLVD Place boasts over 200,000 square feet of retail and office. The Frost Bank regional office opened in BLVD Place in the Spring of 2014, while the new Whole Foods Market opened in November 2014. The Galleria Mall began reconstruction and renovation valued at \$250,000,000 at the corner of Westheimer and Sage. Once completed, an additional 40,000 square feet will be added to the mall.

Hotel

Uptown currently has 31 first quality hotels in the area, offering more than 7,100 rooms for guests. Ad valorem values for this sector were certified 5% higher in 2015. By December 2015, both Hyatt Regency and the Hyatt Place will add an additional 482 rooms to the Uptown market. Landry's is developing a 35 story mixed-use development call "The Post Oak" which broke ground in August 2015. The new hotel will add an additional 240 rooms when completed in 2017.

The area's RevPAR (revenues per available room) is the \$130.48 and comparable to the Houston Central Business District at \$145.34. The RevPAR for Houston City-wide is \$77.15. Uptown Houston also boasts one of the highest occupancy rates in the city at 77.4%, while the Houston City-wide occupancy rate was 71.4% at the end of the second quarter, 2015.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

MANAGEMENT'S DISCUSSION AND ANALYSIS (*continued*)

Residential

Seven new high-rise residential towers have been built in Uptown in the past eight years. Single-family properties are holding values with some properties increasing slightly. Multi-family developments certified 30% percent higher this year as the tax rolls for some of these newer projects were updated to reflect the completed project. Residential activity continues to grow in the area. Giorgio Borlenghi's Belfiore and Randall Davis's Astoria are both new condominiums which have sold out. Trammel Crow will soon break ground on its 400 unit project, "Alexan 5151". Hanover's 355 unit luxury apartments just completed and is ahead of occupancy projections. Uptown Houston is one of the most prestigious and desirable areas to live.

The economic outlook is positive in Uptown. In 2015, the ad valorem values were up over 6% from the previous year and Uptown remains a viable district. While economic factors (property values, vacancy rates, future development, etc.) impact the size of debt issues, management takes a conservative approach to ensure that adequate resources are available to support the projects within the mandates of the Plan.

Requests for Information

This financial report is designed to provide a general overview of the Harris County Improvement District No. 1's finances for all those with an interest in the government's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to Harris County Improvement District No. 1, 1980 Post Oak Boulevard #1700, Houston, Texas 77056.

BASIC FINANCIAL STATEMENTS

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

STATEMENT OF NET POSITION - GOVERNMENTAL ACTIVITIES

June 30, 2015

Assets

Cash and temporary investments	\$ 7,170,673
Restricted Cash	49,267
Property taxes receivable	133,673
Due from other governments	753,755
Other receivables	12,561
Prepaid expenses	54,767
Capital assets, net of depreciation	<u>1,800,256</u>
Total Assets	<u>9,974,952</u>

Deferred Outflows of Resources

Deferred Charge on Refunding	<u>164,614</u>
Total Deferred Outflows of Resources	<u>164,614</u>

Liabilities

Accounts payable and accrued expenses	926,963
Accrued interest	79,760
Noncurrent liabilities:	
Due in less than one year	795,000
Due in more than one year	<u>8,298,691</u>
Total Liabilities	<u>10,100,414</u>

Net Position

Investment in capital assets	1,800,256
Restricted for debt service	1,148,835
Unrestricted	<u>(2,909,939)</u>
Total Net Position	<u>\$ 39,152</u>

See notes to the Financial Statements.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

STATEMENT OF ACTIVITIES - GOVERNMENTAL ACTIVITIES

For the Year Ended June 30, 2015

<u>Functions/Programs</u>	<u>Expenses</u>	<u>Program Revenue</u>		<u>Net (Expense) Revenue and Changes in Net Position</u>
		<u>Charges for Services</u>	<u>Capital Grants</u>	
General and administrative	\$ 2,804,728	\$ 1,340,002	\$ -	\$ (1,464,726)
Traffic Control	1,739,788	-	-	(1,739,788)
Maintenance and beautification	1,781,585	78,230	-	(1,703,355)
Planning and engineering	138,446	-	-	(138,446)
Marketing and communication	787,931	-	-	(787,931)
Interest on long-term debt and other charges	239,644	-	-	(239,644)
Economic development	90,500	-	-	(90,500)
Construction on behalf of the City of Houston	-	-	4,688,550	4,688,550
Transfers to other governments - Uptown Development Authority	4,688,550	-	-	(4,688,550)
Total activities	<u>\$ 12,271,172</u>	<u>\$ 1,418,232</u>	<u>\$ 4,688,550</u>	<u>(6,164,390)</u>

General revenues:

Property taxes	7,619,248
Unrestricted investment earnings	15,723
Total general revenues and transfers	<u>7,634,971</u>
Change in net position	1,470,581
Net position - beginning	<u>(1,431,429)</u>
Net position - ending	<u>\$ 39,152</u>

See notes to the Financial Statements.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

BALANCE SHEET - GOVERNMENTAL FUNDS

June 30, 2015

	General Fund	Capital Projects	Debt Service	Total Governmental Funds
Assets				
Cash	\$ 5,873,489	\$ 136,013	\$ 1,161,171	\$ 7,170,673
Restricted Cash	49,267	-	-	49,267
Taxes receivable	103,531	-	30,142	133,673
Due from other funds	351,815	-	42,370	394,185
Due from other governments	233,858	469,862	-	703,720
Other receivables	-	50,035	-	50,035
Due from others	12,561	-	-	12,561
Prepaid items	54,767	-	-	54,767
Total Assets	<u>\$ 6,679,288</u>	<u>\$ 655,910</u>	<u>\$ 1,233,683</u>	<u>\$ 8,568,881</u>
Liabilities and Deferred Inflows				
Liabilities:				
Accounts payable	\$ 407,771	514,104	5,088	\$ 926,963
Due to other funds	-	394,185	-	394,185
Total Liabilities	<u>407,771</u>	<u>908,289</u>	<u>5,088</u>	<u>1,321,148</u>
Deferred Inflows of Resources				
Unavailable Revenues - Property Taxes	<u>103,531</u>	<u>-</u>	<u>30,142</u>	<u>133,673</u>
Total Deferred Inflows of Resources	<u>103,531</u>	<u>-</u>	<u>30,142</u>	<u>133,673</u>
Fund balances:				
Restricted for:				
Nonspendable	54,767	-	-	54,767
Restricted	-	-	1,198,453	1,198,453
Unassigned	6,113,219	(252,379)	-	5,860,840
Total Fund Balances	<u>6,167,986</u>	<u>(252,379)</u>	<u>1,198,453</u>	<u>7,114,060</u>
Total Liabilities, Deferred Inflows of Resources, and Fund Balances	<u>\$ 6,679,288</u>	<u>\$ 655,910</u>	<u>\$ 1,233,683</u>	<u>\$ 8,568,881</u>

See notes to the Financial Statements.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

**RECONCILIATION OF THE GOVERNMENTAL FUNDS
BALANCE SHEET TO THE STATEMENT OF NET POSITION**

June 30, 2015

Total fund balance, governmental funds \$ 7,114,060

Amounts reported for governmental activities in the Statement of Net Position are different because:

Capital assets used in governmental activities are not financial resources and, therefore, are not reported as assets in governmental funds.

Capital Assets at historical cost	16,052,719	
Less accumulated depreciation	<u>(14,252,463)</u>	
Change due to capital assets		1,800,256

Property taxes receivable and related penalties and interest have been levied and are due, but are not available soon enough to pay current period expenditures and, therefore, are deferred in the funds.

Property taxes receivable	81,222	
Penalty and interest receivable	<u>52,451</u>	
Change due to property taxes		133,673

Some liabilities and deferred outflows are not due and payable in the current period and are not included in the fund financial statements, but are included in the Statement of Net Position. These are as follows:

Bonds payable	(8,505,000)	
Deferred charge on refunding	164,614	
Unamortized premiums	(490,691)	
Accrued interest	(79,760)	
Compensated absences	<u>(98,000)</u>	
Change due to long-term obligations		<u>(9,008,837)</u>

Net Position of Governmental Activities in the Statement of Net Position \$ 39,152

See notes to the Financial Statements.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

**STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES - GOVERNMENTAL FUNDS**

For the Year Ended June 30, 2015

	<u>General Fund</u>	<u>Capital Projects</u>	<u>Debt Service</u>	<u>Total Governmental Funds</u>
Revenues				
Property taxes	\$ 6,568,905	\$ -	\$ 1,049,120	\$ 7,618,025
Intergovernmental	1,340,002	4,688,550	-	6,028,552
Investment earnings	12,719	1,132	1,872	15,723
Other Income	78,230	-	-	78,230
Total Revenues	<u>7,999,856</u>	<u>4,689,682</u>	<u>1,050,992</u>	<u>13,740,530</u>
Expenditures				
Current:				
Planning and engineering	138,446	-	-	138,446
Traffic control	996,329	-	-	996,329
Maintenance and beautification	1,781,585	-	-	1,781,585
General and administrative	2,792,969	-	-	2,792,969
Marketing and communications	785,431	-	-	785,431
Economic development	90,500	-	-	90,500
Debt Service:				
Principal	-	-	750,000	750,000
Interest and other charges	-	-	289,985	289,985
Capital Outlay	-	553,702	-	553,702
Transfers to other governments - Uptown Development Authority	-	4,688,550	-	4,688,550
Total Expenditures	<u>6,585,260</u>	<u>5,242,252</u>	<u>1,039,985</u>	<u>12,867,497</u>
Excess (deficiency) of Revenues over Expenditures	<u>1,414,596</u>	<u>(552,570)</u>	<u>11,007</u>	<u>873,033</u>
Other Financing Sources/(Uses):				
Transfers in	-	553,702	-	553,702
Transfers out	(553,702)	-	-	(553,702)
Total Other Financing Sources/(Uses)	<u>(553,702)</u>	<u>553,702</u>	<u>-</u>	<u>-</u>
 Net change in Fund Balances	860,894	1,132	11,007	873,033
Fund Balances - beginning of year	5,307,092	(253,511)	1,187,446	6,241,027
Fund Balances - end of year	<u>\$ 6,167,986</u>	<u>\$ (252,379)</u>	<u>\$ 1,198,453</u>	<u>\$ 7,114,060</u>

See notes to the Financial Statements.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES
AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES**

For the Year Ended June 30, 2015

Net change in fund balances - total governmental funds: \$ 873,033

Amounts reported for Governmental Activities in the Statement of Activities are different because:

Governmental funds do not report revenues that are not available to pay current obligations. In contrast, such revenues are reported in the Statement of Activities when earned. The difference is for property taxes and related penalties and interest. 1,223

Governmental funds report capital outlays as expenditures. However, in the Statement of Activities the costs of those assets is allocated over their estimated useful lives and reported as depreciation expense for the period.

Capital outlay expenditures	\$ 553,702	
Depreciation expense	(745,959)	
Change due to capital assets		(192,257)

The issuance of long-term debt provides current financial resources to governmental funds, while the repayment of principal uses current financial resources. However, at the government-wide level these transactions have the effect of increasing or decreasing long-term liabilities.

Principal payment of debt	750,000	
Premium is amortized over the life of the bond	60,021	
Deferred charge on refunding is amortized over the life of the bond	(20,136)	
		789,885

Some expenses reported in the statement of activities do not require the use of current financial resources and are not reported as expenditures in governmental funds. These are as follows:

Change in compensated absences	(11,759)	
Change in interest payable	10,456	
		(1,303)

Change in net position of governmental activities		<u>\$ 1,470,581</u>
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See notes to the Financial Statements.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO THE FINANCIAL STATEMENTS

June 30, 2015

A. Summary of Significant Accounting Policies

The financial statements of Harris County Improvement District No. 1 (“the District”) have been prepared in conformity with generally accepted accounting principles (GAAP) as applied to governmental units. The Government Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and reporting principles. The following is a summary of the most significant policies.

Creation

Harris County Improvement District No. 1 (the “District”) was organized, created, and established pursuant to an act of the 70th Texas State Legislature, effective under the terms and provisions of Article III, Section 52 and Article XVI, Section 59 of the Texas Constitution. The Board of Directors held its organizational meeting on July 18, 1987. The first bonds were sold on June 23, 1993. See Note F for additional information regarding significant legal provisions contained in the legislative act creating the District.

The District's primary activities include managing and financing improvement projects and/or services benefiting the District. These activities include maintenance and beautification of the area, traffic control and transportation projects, special events for the holiday seasons, general planning and engineering, area marketing, major capital improvements and general and administrative services.

Reporting Entity

The District is a political subdivision of the State of Texas, governed by an appointed board, and is considered a primary government. The GASB has established the criteria for determining whether or not an entity is a primary government or a component unit of a primary government. The primary criteria are that it has a separately elected governing body; it is legally separate; and it is fiscally independent of other state and local governments. Under these criteria, the District is considered a primary government and is not a component unit of any other government. Additionally, no other entities meet the criteria for inclusion in the District’s financial statements as component units.

Government-wide and Fund Financial Statements

Government-wide financial statements display information about the District as a whole. These statements focus on the sustainability of the District as an entity and the change in aggregate financial position resulting from activities of the fiscal period. Interfund activity, if any, has been removed from these statements. The government wide statements consist of the *Statement of Net Position* and the *Statement of Activities*.

The *Statement of Activities* demonstrates the degree to which the direct expenses of a given function or segment is offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenue includes: (1) charges to customers or applicants, who purchase, use or directly benefit from goods, services, or privileges provided by a given function or segment and (2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular segment. Taxes and other items not properly included among program revenues are reported as general revenues.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO THE FINANCIAL STATEMENTS *(continued)*

A. Summary of Significant Accounting Policies - continued

Fund financial statements display information at the individual fund level. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for a specific purpose. Each fund is considered to be a separate accounting entity. These fund financial statements are the *Governmental Funds- Balance Sheet* and the *Governmental Funds - Statement of Revenues, Expenditures and Changes in Fund Balances*

The District reports the following major governmental funds:

The *General Fund* is used to account for administrative operations of the District. The principal source of revenue is property taxes. Expenditures include all costs associated with the daily operations of the District.

The *Debt Service Fund* is used to account for the payment of interest and principal on all general long-term debt of the District. The primary source of revenue is provided by contract tax increment revenue.

The *Capital Projects Fund* is used to account for the expenditure of bond proceeds used in the construction of authorized improvement projects.

Measurement Focus and Basis of Accounting

The Government-wide financial statements are reported using the *economic resources measurement focus* and the *accrual basis of accounting*. Revenues are recognized when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available if they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the District considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures are generally recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Receivables

All receivables are reported at their gross value and, where appropriate, are reduced by the estimated portion that is expected to be uncollectible. At June 30, 2015, an allowance for uncollectible property tax accounts was not considered necessary.

Prepaid Items

Certain payments made by the District reflect costs applicable to future accounting periods and are recorded as prepaid items in both the government-wide and fund financial statements.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO THE FINANCIAL STATEMENTS (continued)

A. Summary of Significant Accounting Policies - continued

Capital Assets

Capital assets are reported in the government-wide financial statements. The District defines capital assets as assets with an initial, individual cost of \$5,000 or more and an estimated useful life in excess of one year. Capital assets are recorded at historical cost or estimated historical cost. Donated capital assets are recorded at the estimated fair value at the date of donation. Assets are depreciated over their remaining useful lives using the straight-line method.

Asset	Estimated Useful Lives
Machinery and Equipment	10 - 20 years

Fund Balance / Restricted Assets

The District records reservations for all or portions of governmental fund balances which are legally segregated for specific future use or which do not represent available spendable resources and therefore not available for appropriation. Unassigned fund balance indicates the portion of fund balance which is available for appropriation in future periods. The restricted fund balances for governmental funds represent the amount that has been identified for specific purposes.

The District applies restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net position are available.

The following fund balance classifications describe the relative strength of the spending constraints:

Nonspendable fund balance – amounts that are not in spendable form or are required to be maintained intact. As such, the inventory and prepaid items have been properly classified in the Governmental Funds Balance Sheet.

Restricted fund balance – Amounts that can be spent only for specific purposes because of local, state or federal laws, or externally imposed conditions by grantors or creditors.

Committed fund balance – amounts constrained to specific purposes by the District itself, using its highest level of decision-making authority (i.e. the Board of Directors). To be reported as committed, amounts cannot be used for any other purposes unless the District takes the same highest level of action to remove or change the constraint.

Assigned fund balance – amounts the District intends to use for a specific purpose. Intent can be expressed by the Authority or by an official or body to which the Board of Directors delegates the authority. Funds maybe be assigned by the District’s president or by the Board of Directors for specific purposes through the budget process or agenda items.

Unassigned fund balance – amounts that are available for any purpose. Positive amounts are reported only in the general fund.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO THE FINANCIAL STATEMENTS *(continued)*

A. Summary of Significant Accounting Policies - continued

Fund Balance / Restricted Assets - continued

The District establishes (and modifies or rescinds) fund balance commitments by passage of a resolution. When an expenditure is incurred for purposes for which both restricted and unrestricted fund balance is available, the District considers restricted funds to have been spent first. When an expenditure is incurred for which committed, assigned, or unassigned fund balances are available, the District considers amounts to have been spent first out of committed funds, then assigned funds, and finally unassigned funds. The District has nonspendable, restricted and unassigned fund balances as of June 30, 2015.

Deferred Outflows/Inflows of Resources

In addition to assets, the statement of financial position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, *deferred outflows of resources*, represents a consumption of net position that applies to a future period(s) and so will *not* be recognized as an outflow of resources (expense/ expenditure) until then. The District only has one item that qualifies for reporting in this category. It is the deferred charge on refunding reported in the government-wide statement of net position. A deferred charge on refunding results from the difference in the carrying value of refunded debt and its reacquisition price. This amount is deferred and amortized over the shorter of the life of the refunded or refunding debt. At year-end, the District had a deferred outflow of \$164,614.

In addition to liabilities, the governmental funds balance sheet will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, *deferred inflows of resources*, represents an acquisition of fund balance that applies to a future period(s) and so will *not* be recognized as an inflow of resources (revenue) until that time. The District has unavailable property taxes including penalty and interest of \$133,673 that qualifies for reporting in this category, which arise only under a modified accrual basis of accounting.

Interfund Activity

During the course of operations, transactions occur between individual funds. This can include internal transfers, payables and receivables. This activity is combined as internal balances and is eliminated in both the government-wide and fund financial statements.

Compensated Absences

The District's employees earn vacation leave, which may either be taken or accumulated, up to certain amounts, until paid upon termination or retirement. The amounts are recorded as a liability in the *Statement of Net position*.

Use of Estimates

The preparation of financial statements, in conformity with generally accepted accounting principles, requires management to make estimates and assumptions that affect the amounts reported in the financial statements. Actual results could differ from those estimates.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO THE FINANCIAL STATEMENTS (continued)

B. Deposits and Investments

As of June 30, 2015, the District's cash was comprised of the following:

	Carrying Value	Bank Balance
Money market funds	\$ 7,170,673	\$ 9,399,273
Restricted Cash	49,267	49,267
	<u>\$ 7,219,940</u>	<u>\$ 9,448,540</u>

The cash deposits were entirely covered by the Federal Deposit Insurance Corporation (FDIC) up to \$250,000 or by pledged collateral held by the District's agent banks in the District's name.

As of June 30, 2015, the District had no investments.

Authorized Investments

The District is authorized by the *Public Funds Investment Act* (Chapter 2256, Texas Government Code) to invest in the following: (1) obligations of the United States or its agencies and instrumentalities, (2) direct obligations of the State of Texas or its agencies and instrumentalities, (3) certain collateralized mortgage obligations, (4) other obligations, which are unconditionally guaranteed or insured by the State of Texas or the United States or its agencies or instrumentalities, (5) certain A rated or higher obligations of states and political subdivisions of any state, (6) bonds issued, assumed or guaranteed by the State of Israel, (7) insured or collateralized certificates of deposit, (8) certain fully collateralized repurchase agreements, (9) bankers' acceptances with limitations, (10) commercial paper rated A-1 or P-1 or higher and a maturity of 270 days or less, (11) no-load money market mutual funds and no-load mutual funds, with limitations, (12) certain guaranteed investment contracts, (13) certain qualified governmental investment pools and (14) a qualified securities lending program.

The District has adopted a written investment policy to establish the principles by which the District's investment program should be managed. This policy further restricts the types of investments in which the District may invest.

Investment Credit and Interest Rate Risk

Investment credit risk is the risk that the investor may not recover the value of an investment from the issuer, while interest rate risk is the risk that the value of an investment will be adversely affected by changes in interest rates. The Authority's investment policies do not address investment credit and interest rate risk beyond the rating and maturity restrictions established by state statutes.

Restricted Cash

As discussed in Note I, the District has entered into an agreement for deferred compensation for certain employees, the amount in the plan's account is restricted for additional compensation to certain employees after their retirement, or a death benefit to the employees' designated beneficiaries after their deaths.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO THE FINANCIAL STATEMENTS (continued)

C. Capital Assets

A summary of changes in capital assets, for the year ended June 30, 2015, follows:

	Beginning Balance	Additions	Retirements and Transfers	Ending Balance
Capital assets, not being depreciated				
Construction in progress	\$ 356,000	\$ -	\$ (356,000)	\$ -
Total Capital assets, not being depreciated	356,000	-	(356,000)	-
Capital assets, being depreciated:				
Machinery and equipment	15,143,017	553,702	356,000	16,052,719
Less accumulated depreciation	(13,506,504)	(745,959)	-	(14,252,463)
Total Capital assets, net of depreciation	1,636,513	(192,257)	356,000	1,800,256
Governmental Capital Assets	\$ 1,992,513	\$ (192,257)	\$ -	\$ 1,800,256

Depreciation was charged to functions of the District as follows:

Traffic control	\$ 743,459
Marketing and communication	2,500
Total depreciation expense	<u>\$ 745,959</u>

D. Long-Term Liabilities

During the year, the District's long-term liabilities changed as outlined below:

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Bonds payable	\$ 9,255,000	\$ -	\$ (750,000)	\$ 8,505,000	\$ 795,000
Unamortized premiums	550,712		(60,021)	490,691	-
Compensated absences	86,241	111,798	(100,039)	98,000	-
	<u>\$ 9,891,953</u>	<u>\$ 111,798</u>	<u>\$ (910,060)</u>	<u>\$ 9,093,691</u>	<u>\$ 795,000</u>

Bonds payable as of June 30, 2015 consists of the following:

Series	Amount Outstanding	Original Issue	Interest Rate
Refunding Bonds, Series 2013	8,505,000	9,300,000	1.875%-4.00%
Total	<u>\$ 8,505,000</u>		

During the fiscal year ended June 30, 2013, the District issued 2013 Refunding Bonds, refunding a portion of the 1999 and the 2004 bond issues. The reacquisition price exceeded the net carrying amount of the old debt by \$204,886. This resulting deferred outflow is amortized over the life of the Bond.

	Previous Balance	Current Year	Year End Balance
Refunding difference 2013 Issue	184,750	(20,136)	164,614
	<u>\$ 184,750</u>	<u>\$ (20,136)</u>	<u>\$ 164,614</u>

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO THE FINANCIAL STATEMENTS (continued)

D. Long-Term Liabilities - continued

Payment of principal and interest on the bonds is to be provided from tax levies on properties within the District. As the bonds are unlimited tax bonds, no other funds of the District have been pledged for debt service requirements. Investment income realized by the Debt Service Fund, from investment of excess funds, will be used to pay outstanding bond principal and interest. The District is in compliance with all significant requirements and restrictions contained in its bond resolution.

Annual debt service requirements to retire these outstanding bonds are as follows:

Year Ending June 30,	Principal	Interest	Total
2016	\$ 795,000	\$ 258,475	\$ 1,053,475
2017	840,000	228,750	1,068,750
2018	880,000	202,663	1,082,663
2019	915,000	176,675	1,091,675
2020	950,000	148,700	1,098,700
2021	990,000	119,600	1,109,600
2022	1,020,000	89,450	1,109,450
2023	1,045,000	58,475	1,103,475
2024	1,070,000	21,400	1,091,400
	<u>\$ 8,505,000</u>	<u>\$ 1,304,188</u>	<u>\$ 9,809,188</u>

A summary of District Bonds authorized, but unissued at June 30, 2015 follows:

<u>Purpose</u>	<u>Date Authorized</u>	<u>Amount Authorized</u>	<u>Amount Unissued</u>
Stimulation and development of transportation	05/30/92	\$ 75,000,000	\$ 59,915,000
Conservation and preservation of natural resources	05/30/92	25,000,000	22,005,000
Improvement projects payable from assessments	05/30/92	25,000,000	25,000,000
Improvement projects for economic diversification	11/20/93	25,000,000	25,000,000
		<u>\$ 150,000,000</u>	<u>\$ 131,920,000</u>

E. Property Taxes

On May 30, 1992, the voters of the District authorized the District's Board of Directors to levy taxes annually for use in financing general operations (maintenance tax) limited to \$0.25 per \$100 of assessed property valuation. The Harris County Appraisal District determines all property valuations and exempt status, if any. The District's bond resolution requires that property taxes be levied for use in paying interest and principal on long-term debt and for use in paying costs incurred in assessment and collection of these taxes. Taxes levied for debt service and related costs are without limitation as to rate or amount.

The District has contracted with the Harris County Tax Assessor/Collector for its tax levy and collection functions. A tax lien attaches to properties within the District on January 1 of each year when property valuations for use in levying taxes are established. Taxes levied are generally billed in October and are due upon receipt of the tax bill. Penalty and interest are charged if taxes are not paid by January 31. There is an additional 15% penalty charged on accounts delinquent after July 1, which generally is payable to the District's delinquent tax attorney.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO THE FINANCIAL STATEMENTS (continued)

E. Property Taxes – continued

Property taxes are collected based on rates adopted in the year of the levy. The District’s fiscal year ended June 30, 2015, was financed through the 2014 tax levy. The District levied property taxes of \$0.14345 per \$100 of assessed value, of which \$0.12369 was allocated to maintenance and operations and \$0.01976 was allocated to debt service. The resulting tax levy was on the adjusted taxable value of \$5,321,828,968.

Taxes receivable, at June 30, 2015, consisted of the following:

Current year taxes receivable	\$	25,229
Delinquent taxes receivable		<u>55,993</u>
		81,222
Penalty and interest receivable		<u>52,451</u>
Total property taxes receivable	\$	<u><u>133,673</u></u>

F. Significant Legal Provisions of Legislative Act Creating District

As discussed in Note A above, the District has been established pursuant to an act of the Texas State Legislature. Significant legal provisions of this act are summarized below.

District Boundaries

The Act provides specifically for boundaries of the District, which includes the Uptown Houston area. The Uptown Houston area is also known as the Galleria-Post Oak area in Houston, Texas. The District may annex additional land area in accordance with Chapter 54 of the Texas Water Code. On May 22, 2013, Harris County Improvement District No. 1 adopted an Order Adding Land (responding to a petition of the landowners) adding 33.99 acres of land (located in the vicinity of the intersection of US 59 and IH 610) to the District.

Texas Commission on Environmental Quality Involvement

The Act provides that the Texas Commission on Environmental Quality is to appoint District Directors. The Directors are to serve staggered four-year terms. Additionally, the Texas Commission on Environmental Quality must approve the issuance of any bonded indebtedness for the purposes of providing water, sewer or drainage facilities within the District. No other District activities are subject to the jurisdiction of the Texas Commission on Environmental Quality.

General and Specific Powers of the District

The Act provides general powers to the District subject to general laws and regulations of the state applicable to conservation and reclamation districts created under Article XVI, Section 59 of the Texas Constitution and road districts and road utility districts created pursuant to Article III, Section 52, of the Texas Constitution, including those conferred by Chapter 54 of the Water Code and Chapter 13, Acts of the 68th legislature, 2nd Called Session, 1984 (Article 6674r-1, Vernon’s Texas Civil Statutes).

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO THE FINANCIAL STATEMENTS (continued)

F. Significant Legal Provisions of Legislative Act Creating District – continued

General and Specific Powers of the District - continued

Additional specific powers and duties are provided for in the act, which include the financing of improvement projects and/or services for the benefit of the District. Specific types of improvement projects are provided for in the act and include the acquisition of land in connection with the improvements. Eminent domain powers are specifically prohibited by the act. Improvement projects and/or services may be financed in whole or in part by the levy and collection of special assessments or property taxes on property in the area. The act also provides that maintenance taxes may be levied after voter approval.

The Act provides for the method by which the District must petition, provide notice and hold public hearings prior to the financing of the improvement projects and/or services.

The Act also provides for the issuance of voter-approved bonded indebtedness to finance improvement projects and/or services. Specific guidelines in the act provide for the repayment of bonds, which might be issued, as well as the use of bond proceeds, available security that can be pledged in issuing the bonds and refunding capabilities for outstanding bonds.

Director Bonds

The Act requires that each Director appointed execute a bond for \$10,000 payable to the District and conditioned on faithful performance of his or her duties. All bonds of the Directors shall be approved by the Board.

G. Operating Agreement - Uptown Development Authority

The District has entered into an operating agreement with Uptown Development Authority (the “Authority”). The Authority is a component unit of the City of Houston formed to carry on improvements in the Uptown Houston area. The governing boards of both the District and the Authority have common members. It is the intent of both governing boards to maintain separately controlled operating entities. The agreement calls for the District to perform services as and when requested by the Authority Board. The services may consist of general administrative support, project management and development, consultant management, and other services as may be deemed necessary. The District is the recipient of federal grants for pedestrian and intersection improvements within the District. Additionally, the Authority has an approved capital improvement plan which includes pedestrian and intersection improvements. These two entities will work in conjunction with the Authority providing the local match and the implementation of the project while the District will provide the grant funds (see Note N). Financial information regarding the Authority can be obtained from Uptown Development Authority, 1980 Post Oak Boulevard #1700, Houston, Texas 77056.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO THE FINANCIAL STATEMENTS (continued)

G. Operating Agreement - Uptown Development Authority - continued

Financing Agreement - Uptown Development Authority

The District has a Finance Agreement with the Uptown Development Authority (The UDA) in which the Authority could borrow up to \$3.5 million, which is to be repaid by the Authority's fiscal year-end (June 30, 2015). While this agreement is still in place, the Authority did not make use of requesting funds from the District. This agreement is reviewed and approved annually by both Boards of Directors.

H. Pension Plan

For the benefit of its employees, the District provides discretionary contributions to a simplified employee pension plan, meeting the requirements of Internal Revenue Code Section 408(k). For the year ended June 30, 2015, the District contributed \$135,700 to the plan.

I. Deferred Compensation

During the fiscal year ended June 30, 2015, the district entered into a Retirement Plan governed by the provisions of Section 457(f) of the Internal Revenue Code of 1986, as amended. Each year, the District's Board determines the contribution to be made for additional compensation to certain eligible employees after their retirement, or a death benefit to the employees' designated beneficiaries after their deaths. The amount in the Retirement Plan as of June 30, 2015 is \$49,267.

J. Risk Management

The District is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; and personal injuries. The risk of loss is covered by commercial insurance. There have been no significant reductions in insurance coverage. Settlement amounts have not exceeded insurance coverage for current year or the three prior years.

K. Budget Overages

The Schedule of Revenues, Expenditures and Changes in Fund Balances – Budget to Actual presents budget overages in certain expenditures. Maintenance and beautification actual expenditures exceeded budgeted expenditures due to flood repairs to esplanades. General and Administrative expenditures exceeded the budget due to additional legal services for oversight of the rights-of-way acquisition and numerous open records requests. Marketing and communications actual expenditures exceeded the budget due to public relations and communications regarding the Post Oak Boulevard project. Economic Development actual expenditures exceeded the budget due to economic studies for the Uptown area. Overall the District operated with a positive budget variance.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO THE FINANCIAL STATEMENTS (continued)

L. Deficit Fund Balance

A deficit fund balance of \$252,379 exists in the Capital Projects fund as of June 30, 2015. The deficit fund balance is primarily a result of previous transfers to the operating fund to cover project design costs during that period. Management plans to reduce this deficit with the December 2015 new bond issue.

M. Tax Increment Reinvestment Zone

During the current and prior years, the District incurred certain planning expenditures related to the Tax Increment Reinvestment Zone No. 16 of the City of Houston (TIRZ). The TIRZ is located on property generally within the District’s service area. During the year ended June 30, 2015, the District received \$1,340,002 from the TIRZ for reimbursement of administration costs, project management costs and traffic and mobility costs.

N. Federal Grants

The District is a recipient of a federal grant for pedestrian and intersection improvements: Congestion Mitigation and Air Quality (CMAQ) 80/20 Grant and a Congressional appropriated Discretionary Grant. In accordance with the operating agreement with the Uptown Development Authority (UDA); the grant funds are used to fund the UDA’s capital improvement plan. The UDA expends all funds for purposes of the grant, including a 20% local matching requirement under the CMAQ grant terms. All grant revenues are recognized by the District based on the UDA spending and are then paid to the UDA as a reimbursement for grant related spending.

A summary of grant activity through June 30, 2015, is shown below along with similar information for the total grant.

<u>Funding Source</u>	<u>Amounts</u>	
	<u>Actual through June 30, 2015</u>	<u>Total Grant</u>
Congestion Mitigation Air Quality Federal (CMAQ) Grant (80%)	\$ 16,525,009	\$ 15,124,994
Congressional Appropriated Discretionary Grant	2,464,244	2,665,864
	<u>\$ 18,989,253</u>	<u>\$ 17,790,858</u>

The CMAQ and the Discretionary Grant both require a 20 percent match, which is made by the UDA. For the cumulative period ending June 30, 2015, the UDA provided the required local match of \$1,239,638.

O. Related Party Transactions

Mizington Incorporated

During the reporting period, the District entered into a service agreement with Mizington Incorporated for professional services. The Mizington employees are former District employees. Mizington was created to provide employees with the option to contribute to social security as District employees participate in a government pension plan and therefore cannot contribute to social security.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO THE FINANCIAL STATEMENTS *(continued)*

O. Related Party Transactions - continued

Uptown Development Authority

The Authority has an approved capital improvement plan which includes the reconstruction of Post Oak Boulevard. This Authority project requires the purchase of rights-of-way along Post Oak Boulevard. While the Authority is the purchaser, there are some parcels along the Boulevard that are owned and/or affiliated by/with members of the District board.

As public agencies, the District and the Authority are governed by strict laws and regulations on how property is acquired for public projects. During the reporting period and subsequent, the Authority began the process of purchasing right-of-way parcels for the purpose of reconstructing Post Oak Boulevard. Two parcel purchases involved related party transactions with members of the District Board of Directors.

On June 30, 2015 the Authority purchased a parcel of land from Weingarten Realty Investors (a publicly traded company on the NYSE). A District board member is a former Vice Chairman/COO of Weingarten (retired in 2008) and current shareholder. Subsequent to the fiscal year end on November 13, 2015, the Authority purchased a parcel of land from S 2007 Investment Limited Partnership and T 2007 Investment Limited Partnership (Hines related entities) in which a District board member is an employee.

P. Subsequent event

In December 2015, the District authorized the issuance of \$20,365,000 Unlimited Tax Bonds, Series 2015.

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REQUIRED SUPPLEMENTARY INFORMATION

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

**SCHEDULE OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCES - BUDGET TO ACTUAL**

June 30, 2015

	Original Budget	Final Budget	Actual	Variance with Final Budget Positive/ (Negative)
Revenues				
Property taxes	\$ 5,789,737	\$ 5,789,737	\$ 6,568,905	\$ 779,168
Intergovernmental	1,944,800	1,944,800	1,340,002	(604,798)
Shelter program (Metro)	33,263	33,263	-	(33,263)
Investment earnings	12,146	12,146	12,719	573
HGAC Grants	5,000,000	5,000,000	4,688,550	(311,450)
Miscellaneous	-	-	78,230	78,230
Total Revenues	12,779,946	12,779,946	12,688,406	(91,540)
Expenditures				
Current:				
Planning and engineering	675,000	675,000	138,446	536,554
Traffic control	1,008,200	1,008,200	996,329	11,871
Maintenance and beautification	1,711,350	1,711,350	1,781,585	(70,235)
General and administrative	2,653,689	2,653,689	2,792,969	(139,280)
Marketing and communications	590,000	590,000	785,431	(195,431)
Economic development	80,000	80,000	90,500	(10,500)
Transfer of HGAC Grants to UDA	5,000,000	5,000,000	4,688,550	311,450
Total Expenditures	11,718,239	11,718,239	11,273,810	444,429
Excess (deficiency) of revenues over expenditures	1,061,707	1,061,707	1,414,596	(352,889)
Other Financing Sources (Uses)				
Transfers out	-	-	(553,702)	(553,702)
Total Other Financing Sources (uses)	-	-	(553,702)	(553,702)
Net change in fund balance	1,061,707	1,061,707	860,894	(200,813)
Fund balance - beginning of year	5,307,092	5,307,092	5,307,092	-
Fund balance - end of year	\$ 6,368,799	\$ 6,368,799	\$ 6,167,986	\$ (200,813)

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION
June 30, 2015

Budgets and Budgetary Accounting

A non-appropriated budget is adopted for the General Fund by the District's Board of Directors. The budget is considered a planning tool and does not constitute legal spending limit authority. The budget is prepared using the same method of accounting as for the financial reporting except that the General Fund budget includes federal grant revenues and the related transfers. For financial reporting purposes, the federal grant revenues (included in HGAC grants in the preceding schedule) and the related transfers to UDA are reported in the Capital Projects Fund as an intergovernmental revenue and as an expenditure, respectively.

Prior to July 1, 2014, the District adopted its annual budget, or Original Budget, any amendments to the budget are made throughout the year but prior to June 30, 2015 to present a Final Budget as of June 30, 2015. There were no amendments to the budget during the fiscal year.

INDEPENDENT AUDITOR’S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the Board of Directors
Harris County Improvement District No. 1
Houston, Texas

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the governmental activities and each major fund of Harris County Improvement District No. 1’s (the “District”) as of and for the year ended June 30, 2015, and the related notes to the financial statements, which collectively comprise the District’s basic financial statements, and have issued our report thereon dated January 18, 2016.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the District’s internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District’s internal control. Accordingly, we do not express an opinion on the effectiveness of the District’s internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity’s financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

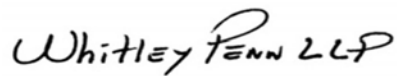
To the Board of Directors
Harris County Improvement District No. 1

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the District's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

A handwritten signature in black ink that reads "Whitley Penn LLP". The signature is written in a cursive, flowing style.

Houston, Texas
January 18, 2016

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR FEDERAL PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE
REQUIRED BY *OMB CIRCULAR A-133***

To the Board of Trustees
Harris County Improvement District No. 1
Houston, Texas

Report on Compliance for Each Major Federal Program

We have audited Harris County Improvement District No. 1's (the "District") compliance with the types of compliance requirements described in the OMB Circular A-133 Compliance Supplement that could have a direct and material effect on each of the District's major federal programs for the year ended June 30, 2015. The District's major federal program is identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal program.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the District's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the District's compliance.

To the Board of Directors
Harris County Improvement District No. 1

Opinion on Each Major Federal Program

In our opinion, Harris County Improvement District No. 1 complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on its major federal program for the year ended June 30, 2015.

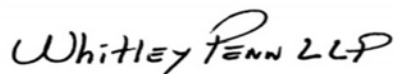
Report on Internal Control Over Compliance

Management of the District is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the District's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the District's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.



Houston, Texas
January 18, 2016

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2015

I. Summary of Auditors' Results

Financial Statements

Type of auditors' report issued	Unmodified
Internal control over financial reporting:	
Material weakness (es) identified?	No
Significant deficiency (ies) identified that are not considered to be material weaknesses?	None reported
Noncompliance material to the financial statements noted?	No

Federal Awards

Internal controls over major programs:	
Material weakness (es) identified?	No
Significant deficiency (ies) identified that are not considered to be material weaknesses?	None reported
Type of auditor's report issued on compliance for major programs:	Unmodified
Any audit findings disclosed that are required to be reported in accordance with section .510(a) of OMB Circular A-133	None

Identification of Major Programs:

Name of Federal Program	CFDA Number
Federal Transit Administration	
Federal Transit – Formula Grants	20.507
Dollar Threshold Considered Between Type A and Type B Federal Programs	\$300,000
Auditee qualified as low-risk auditee?	Yes

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

**SCHEDULE OF FINDINGS AND QUESTIONED COSTS *(continued)*
FOR THE YEAR ENDED JUNE 30, 2015**

II. Financial Statement Findings

No current year findings.

III. Federal Award Findings and Questioned Costs

No current year findings.

IV. Summary Schedule of Prior Audit Findings

No prior year findings.

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2015

<u>Federal Grantor/ Pass Through Grantor/ Program Title</u>	<u>CFDA Number</u>	<u>Grantor Number</u>	<u>Federal Grant Expenditures</u>
Department of Transportation			
<i>Federal Transit Formula Grants -</i>			
<i>Pedestrian/Transit Improvement Program</i>	20.507	TX-95-X005-03	2,245,573
<i>Post Oak Dedicated Bus Lanes/Trst Ctr</i>	20.507	TX-95-X077-00	2,442,977
Total Department of Transportation			<u>4,688,550</u>
Total Federal Awards			<u>\$ 4,688,550</u>

HARRIS COUNTY IMPROVEMENT DISTRICT NO. 1

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

Note 1 - Summary of Significant Accounting Policies

The District accounts for federal funding using the modified accrual method of accounting. This basis of accounting recognizes revenues in the accounting period in which they become susceptible to accrual, i.e. both measurable and available, and expenditures in the accounting period in which the liability is incurred, if measurable, except for compensated absences, claims and judgments which are recognized when the obligations are expected to be liquidated with expendable available financial resources. Capital items for grant purposes are treated as expenses in the schedule of expenditures of federal awards.

Federal grant funds are considered to be earned to the extent of expenditures made under the provisions of the grant, and, accordingly, when such funds are received, they are recorded as unearned revenues until earned. Generally, unused balances are returned to the grantor at the close of specified project periods.

Note 2 - Basis of Presentation

The accompanying schedule of expenditures of federal awards (the "Schedule") includes the federal grant activity of the District under programs of the federal government for the year ended June 30, 2015. The information in this schedule is presented in accordance with the requirements of the Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Government, and Non-Profit Organizations*. Because the schedule presents only a selected portion of the operations of the District, it is not intended to and does not present the financial position, changes in net positions or cash flows of the District.